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IN THE

Supreme Court of The United States

OCTOBER TERM, 1991

NL INDUSTRIES, INC.

Petitioner,

V.

GHR ENERGY CORPORATION,
SOUTHERN STATES EXPLORATION, INC.
AND S.A. HOLDITCH & ASSOCIATES, INC.,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

JOHN C. NABORS
Counsel of Record for Respondents GHR Energy Corporation and Southern States Exploration, Inc.
1200 Texas Commerce Tower
2200 Ross Avenue
Dallas, Texas 75201
(214) 220-4800 (Telephone)
(214) 220-4899 (Telecopier)

Of Counsel
MICHAEL P. STEVENS
140 Cypress Station Dr.
Suite 200
Houston, Texas 77090
(713) 444-1199 (Telephone)
(713) 444-2654 (Telecopier)

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RULE 29.1 LISTING

GHR Energy Corporation, n/k/a TransAmerican Natural Gas Corporation is the parent corporation. Southern States Exploration, Inc. is a wholly owned subsidiary of TransAmerican Natural Gas Corporation. Other than their wholly owned subsidiaries, neither TransAmerican Natural Gas Corporation nor Southern States Exploration, Inc. has any subsidiaries.

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Respondents GHR Energy Corporation, Southern States Exploration, Inc. respectfully pray that the Court deny the Petition for Writ of Certiorari to review the judgment and opinion of the United States Court of Appeals for the Fifth Circuit entered on September 10, 1991.

SUMMARY OF ARGUMENT

NL asserts that the Fifth Circuit's holding that punitive damages are not recoverable as an administrative expense conflicts with decisions of this Court and a number of other circuits. The cases upon which NL relies, however, stand only for the proposition that actual compensatory damages in tort are recoverable as administrative expenses. The cited decisions do not support the proposition that punitive damages are recoverable as administrative expenses. On the contrary, a number of trial and appellate courts have held that punitive damages, unlike compensatory actual damages in tort, are not recoverable as administrative expenses in bankruptcy.

Following NL's original complaint, TransAmerican removed this action to the bankruptcy court. On NL's own motion, the reference of this matter was withdrawn and the case transferred back to the district court. The district court exercised jurisdiction over this matter pursuant to 28 U.S.C. §1334 and properly addressed NL's entitlement to punitive damages in bankruptcy. The Fifth Circuit's *de novo* determination properly addressed NL's entitlement to punitive damages.

NL's original and first amended complaints assert negligence on a part of both S.A. Holditch & Associates, Inc. and TransAmerican in Holditch's activities as an arbiter. Texas law, however, holds that an arbiter's decision is final and not subject to a negligence attack, but only actions for fraud, misconduct and gross mistake. NL's attempts to include these latter causes of action through a second amendment was denied by the district court and properly affirmed on appeal.

ARGUMENT

I. The Fifth Circuit's Holding Regarding Punitive Damages Neither Conflicts With Decisions of this Court, Nor Represents an Important Question of Federal Law Which Should be Addressed by This Court

The thrust of NL's argument is that the decisions and underlying policies in *Reading Co. v. Brown*, 391 U.S. 471 (1968) and *Boteler v. Ingels*, 308 U.S. 57 (1939) provide for the recovery as administrative expenses of punitive damages attendant to post-petition tort claims. NL contends that the Fifth Circuit's holding regarding punitive damages conflicts with *Reading* and *Boteler*, and with decisions from other circuits.

In *Reading*, a realty corporation filed a petition for an arrangement under Chapter XI of the old Bankruptcy Act. Respondent was appointed receiver to continue operation of the debtor's business, leasing an industrial building. During the arrangement, fire destroyed the building and spread to adjoining businesses, causing extensive, real and personal property damage. Petitioner and others filed claims in the arrangement based on negligence of the respondent.

Subsequently, the realty company was adjudicated a bankrupt under Chapter XI and the petitioners' claims became claims for administrative expenses. The question presented to this Court was "whether the negligence of a receiver administrating an estate under Chapter XI arrangement gives rise to an 'actual and necessary' cost of operating the debtor's business" 391 U.S. at 476. In concluding that the post-petition tort damages were recoverable as administrative expenses, the Court relied

heavily on the Act's statutory objective of fairness to all persons having claims against the debtor.

Reading does not, however, stand for the proposition that punitive damages are recoverable as an administrative expense in bankruptcy. Although the opinion is not explicit, a close reading shows that petitioner was seeking to recover its monetary losses for property damage and was not seeking the imposition of punitive damages. Specifically, the issue of recovery of punitive damages is nowhere addressed in the opinion, and is not central to the rationale. Moreover, that *Reading* addressed only recovery for direct out-of-pocket expenses brought about by a post-petition tort finds support in many of NL's cited cases. *See, e.g., In re: E.A. Nord Co., Inc.*, 78 B.R. 289 (Bankr. W.D. Wash. 1987)("The Court found that the fire resulted from the receiver's negligent operation of the business, and awarded claimants an administrative expense claim for the *property damage* arising out of these negligent acts.") (emphasis added).

NL cites the Court to a number of cases, all of which are distinguishable on their facts and none of which refer to the recovery of punitive damages as an administrative expense. In *Carter-Wallace, Inc. v. Davis-Edwards Pharmacal Corp.*, 443 F. 2d 867 (2nd Cir. 1971), the appellant court addressed the propriety of injunctive relief associated with a patent infringement case. In a brief mention, the Court cites to *Reading* for the proposition at potential tort damages are recoverable as administrative expenses. The Court never mentions punitive damages, and its brief discussion of *Reading* is nothing more than dicta. In *United States Dept. of Interior v. Elliott*, 761 F.2d 168 (4th Cir. 1985), the Fourth Circuit held that environmental penalty claims accessed against the debtor for post-petition violations of the Surface Mining Control and Reclamation Act of 1977 were recoverable as administrative expenses. A

review of the language of the act and of the Court's opinion reveals, however, that although these damage claims were denoted as penalties, they actually constitute compensatory cleanup costs incurred by the agency. Elliott does not mention and does not stand for the proposition that punitive damages are recoverable as administrative expenses.

In *In re: Charles Bank Laundry, Inc.*, 755 F.2d 200 (1st Cir. 1985) the Court held that a civil fine imposed for violation of a preliminary injunction was recoverable as an administrative expense in bankruptcy. The fine, however, did not constitute punitive or penalty damages, but was merely compensation for attorneys' fees, services and out-of-pocket expenses. This conclusion is consistent with *Reading* and the Fifth Circuit's opinion as well.

In *In re: E.A. Nord Co., supra,* the district court held that an award for fees and costs incurred by a creditor as a result of frivolous claims litigation would constitute an administrative expense claim. Again, however, this award was not punitive in nature, but constituted compensatory damages relating to attorneys' fees and direct out-of-pocket expenses incurred by the creditor.

In *In re: Dennis Ponte, Inc.*, 61 B.R. 296 (Bankr. 9th Cir. 1986), the court was primarily addressing the issue of the necessity of an evidentiary hearing where an objection to the plan of reorganization is based upon feasibility. Although one of the issues relating to that feasibility was the potential collection of post-petition tort damages from the debtor as an administrative expense, the Court neither addressed nor ruled on the propriety of recovery of punitive damages as an administrative expense.

Finally, *Kelly v. Robinson*, 479 U.S. 36 (1986), dealt with the dischargeability of criminal restitution payments in the context of a Chapter 7 liquidation proceeding. The facts in *Kelly* differ substantially from those present in this matter,

and address not whether punitive or penalty type damages are recoverable from an estate, but whether Court ordered criminal restitution is discharged by the filing of a Chapter 7 petition. Although NL suggests that *Kelly* contains policy decisions which mandate a holding other than that of the Fifth Circuit's, the Court held that this exception to discharge was depended upon the "deep conviction that federal bankruptcy courts should not invalidate the results of state criminal proceedings." *Id.* at 47.

Contrary to NL's petition, case law is replete with circumstances where recovery of punitive damages (as an administrative expense or otherwise) has been denied or enjoined. The overriding rationale for punitive expenses is to punish tortfeasors and to deter both them and others from that wrongful conduct. Recovery of punitive damages as an administrative expense would, however, result in disproportionate payments to one creditor to the detriment of others, and would represent a windfall having no relation to compensatory damages. This end result is at direct variance with the policy rationale expressed in *Reading*: That the purpose of the Code is to provide fairly for the compensation of all persons having claims against a debtor. *Accord, In re: A.H. Robins Co.*, 89 B.R. 555, 559 (E.D.Va. 1988) (disallowing punitive damages as an administrative expense); *In re: Johns-Manville Corp.*, 68 B.R. 618, 627 (Bankr. S.D.N.Y. 1986) (holding that punitive damages were not recoverable from trust fund), reversed in part on other grounds, 78 B.R. 407 (S.D.N.Y. 1987), affirmed *sub nom.*, *Kane v. Johns-Manville Corp.*, 843 F.2d 636 (2nd Cir. 1988). *See also, In re: G.A. Corp.*, 681 F.2d 1295, 1301 (11th Cir. 1982) (disallowing claim for punitive damages); *In re: Klefstead*, 95 B.R. 622 (Bankr. W.D. Wis. 1988) (disallowing state post-petition penalties).

II. The Fifth Circuit's Dismissal of NL's Punitive Damages Claim Does Not Deprive NL of Property Without Due Process of Law

NL's contention that the Fifth Circuit's dismissal of the punitive damage claim deprives NL of its due process rights is sophistry. NL is essentially arguing that after filing this action in district court, and moving to withdraw the reference from the bankruptcy court, neither the district court nor the Fifth Circuit had jurisdiction to address the express issues which NL asked them to address.

NL's original complaint was filed in the district court on August 27, 1986. *R. 1.* On October 2, 1986, TransAmerican removed the complaint to bankruptcy court. *R.7.* On October 27, 1986 and December 29, 1986, NL filed motions and briefs seeking to have the reference of TransAmerican's bankruptcy adversaries withdrawn and the case transferred back to the district court. *R. 8 & 12.* On May 21, 1987, the matter was transferred back to the district court, the express relief sought by NL in its motion. *R. 24.*

United States district courts have original jurisdiction over bankruptcy matters pursuant to 28 U.S.C. §1334. This jurisdiction remains the same whether it is exercised by the district court, or exercised by the bankruptcy court on referral. Since the district court had both subject matter and *impersonam* jurisdiction over NL and its claims, the district court did not improperly circumvent the bankruptcy process in denying NL's punitive damage claim. On appeal, the Fifth Circuit properly made a *de novo* determination of NL's entitlement to punitive damages as an administrative claim. There is no error in the court below.

III. The Fifth Circuit's Holding That GHR and Holditch are Insulated From Liability For Negligence Because the Agreement Designated Holditch as an Arbiter Represents the Correct Application of Texas Law

In January 1987, NL added S.A. Holditch & Associates, Inc. as a defendant, alleging that Holditch had failed to use reasonable care in reviewing TransAmerican's fracture designs. The district court found, and the Fifth Circuit agreed, that Holditch had been unambiguously appointed as an arbiter pursuant to Article 4.3.i.1 of the Agreement and as such, could not be found liable under any theory of negligence.

Texas law provides that an arbiter's decision is final and conclusive unless it is proven that the arbiter was "guilty of fraud, misconduct, or such gross mistake as would imply bad faith or failure to exercise an honest judgment." *City of San Antonio v. McKenize Constr. Co.*, 150 S.W. 2d. 989, 996 (1941); *State v. Buckner Constr. Co.*, 704 S.W. 2d. 837, 841 (Tex. App. - Houston [14th Dist.] 1985, writ ref'd n.r.e.). The Fifth Circuit's holding is entirely consistent with these cases and, since NL failed to raise causes of action alleging fraud, misconduct or gross mistake in a timely fashion, they were not properly before the court.

CONCLUSION

Accordingly, GHR Energy Corporation and Southern States Corporation, Inc. respectfully request that the Petition for Writ of Certiorari to the United States Court of Appeals for The Fifth Circuit be denied in all respects.

JOHN C. NABORS
Counsel of Record for Respondents GHR Energy Corporation and Southern States Exploration, Inc.
1200 Texas Commerce Tower
2200 Ross Avenue
Dallas, Texas 75201
(214) 220-4800 (Telephone)
(214) 220-4899 (Telecopier)

Of Counsel

MICHAEL P. STEVENS
140 Cypress Station Dr.
Suite 200
Houston, Texas 77090
(713) 444-1199 (Telephone)
(713) 444-2654 (Telecopier)

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